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No. _____

IN THE

SUPREME COURT OF THE UNITED STATES

October, 1994, Term

PETER A. CRAWFORD, Petitioner,

v.

CHARLES R. LaMantia, Respondent.

PETITION FOR WRIT OF CERTIORARI

To The United States Court of Appeals
for the First Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

(1) Whether a former employee who receives a lump sum distribution from a leveraged Employee Stock Ownership Plan (ESOP) has standing to sue the ESOP's fiduciaries for paying more than adequate consideration for employer stock.

(2) Alternatively, whether an employee who was a participant in the plan at the time of the breach by the ESOP Trustees and a current employee at the time the lawsuit was instituted but has since terminated employment has standing to sue the ESOP's fiduciaries for paying more than adequate consideration for employer stock.

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PARTIES TO THE PROCEEDING

The Plaintiff/Petitioner is Peter A. Crawford. The Defendants/Respondents are Paul D. Littlefield, Irving H. Plotkin and Harland A. Riker, Jr., individually and in their capacity as Trustees of the Arthur D. Little, Inc. Employee Stock Ownership Plan and Trust.

OFFICIAL AND UNOFFICIAL

REPORTS OF OPINIONS DELIVERED

IN THE CASE BY OTHER COURTS

Peter A. Crawford v. Charles R. LaMantia, et al., CA-1038-WF (D. Mass. 1993) (unpublished) [reprinted in A-1 - A-21].

Peter A. Crawford v. Charles R. LaMantia, et al., 34 F.3d 28 (1st Cir. 1994) [reprinted in A-23-A-44].

STATEMENT OF THE GROUNDS ON WHICH THE JURISDICTION OF THIS COURT IS INVOKED

(1) The judgment in this case was entered by the First Circuit on September 14, 1994 (A-45).

(2) A request for rehearing and a rehearing *en banc* was filed by the Petitioner on September 28, 1994 (A-53). The request for rehearing was denied on November 29, 1994, and the suggestion for rehearing *en banc* was also denied on November 29, 1994 (A-62).

(3) Jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254.

CONSTITUTIONAL PROVISIONS, TREATIES, STATUTES, ORDINANCES AND REGULATIONS INVOLVED IN THIS CASE

Statutes:

ERISA § 3(7), 29 U.S.C. § 1002(7) - The term "participant" means any employee or former employee of an employer, or any member or former member of an employee organization, who is or may become eligible to receive a benefit of any type from an employee benefit plan which covers employees of such employer or members of such organization, or whose beneficiaries may be eligible to receive any such benefit.

ERISA § 3(18)B, 29 U.S.C. § 1002(18)(B) - The term "adequate consideration" when used in part 4 of subtitle B means (A) in the case of a security for which there is a generally recognized market, either (i) the price of the security prevailing on a national securities exchange which is registered under section 6 of the Securities Exchange Act of 1934, or (ii) if the security is not traded on such a national securities

exchange, a price not less favorable to the plan than the offering price for the security as established by the current bid and asked prices quoted by persons independent of the issuer and of any party in interest; and (B) in the case of an asset other than a security for which there is a generally recognized market, the fair market value of the asset as determined in good faith by the trustee or named fiduciary pursuant to the terms of the plan and in accordance with regulations promulgated by the Secretary.

ERISA § 403(c)(1), 29 U.S.C. § 1103(c)(1) - Except as provided in paragraph (2), (3), or (4) or subsection (d), or under section 4042 and 4044 (relating to termination of insured plans), or under section 420 of the Internal Revenue Code of 1986 (as in effect on January 1, 1991) the assets of a plan shall never inure to the benefit of any employer and shall be held for the exclusive purposes of providing benefits to participants in the plan and their beneficiaries and defraying reasonable expenses of administration the plan.

ERISA § 404(a)(1)(A), 29 U.S.C. § 1104(a)(1) - Subject to sections 403(c) and (d), 4042 and 4044, a fiduciary shall discharge his duties

with respect to a plan solely in the interest of the participants and beneficiaries and

(A) for the exclusive purpose of:

(i) providing benefits to participants and their beneficiaries; and

(ii) defraying reasonable expenses of administering the plan;

ERISA § 406(a)(1&2) and (b), 29 U.S.C. § 1106(a)(1&2) and (b) -

(a) Except as provided in section 408:

(1) A fiduciary with respect to a plan shall not cause the plan to engage in a transaction, if he knows or should know that such transaction constitutes a direct or indirect:

(A) sale or exchange, or leasing, of any property between the plan and a party in interest;

(B) lending of money or other extension of credit between the plan and a party in interest;

(C) furnishing of goods, services, or facilities between the plan and a party in interest;

(D) transfer to, or use by or for the benefit of, a party in interest, of any assets of the plan; or

(E) acquisition, on behalf of the plan, of any employer security or employer real property in violation of section 407(a).

(2) No fiduciary who has authority or discretion to control or manage the assets of a plan shall permit the plan to hold any employer security or employer real property if he knows or should know that holding such security or real property violates section 407(a).

(b) A fiduciary with respect to a plan shall not:

(1) deal with the assets of the plan in his own interest or for his own account,

(2) in his individual or in any other capacity act in any transaction involving the plan on behalf of a party (or represent a party) whose interests are adverse to the

interests of the plan or the interests of its participants or beneficiaries, or

(3) receive any consideration for his own personal account from any party dealing with such plan in connection with a transaction involving the assets of the plan.

ERISA § 407(d)(6)(A&B), 29 U.S.C. § 1107(d)(6)(A&B) - The term "employee stock ownership plan" means an individual account plan:

(A) which is a stock bonus plan which is qualified, or a stock bonus plan and money purchase plan both of which are qualified, under section 401 of the Internal Revenue Code of 1986, and which is designed to invest primarily in qualifying employer securities, and

(B) which meets such other requirements as the Secretary of the Treasury may prescribe by regulation.

ERISA § 408(b)(3), 29 U.S.C. § 1108(b)(3) - The prohibitions provided in section 406 shall not apply to any of the following transactions:

A loan to an employee stock ownership plan (as defined in section 407(d)(6)), if:

(A) such loan is primarily for the benefit of participants and beneficiaries of the plan, and

(B) such loan is at an interest rate which is not in excess of a reasonable rate.

If the plan gives collateral to a party in interest for such loan, such collateral may consist only of qualifying employer securities (as defined in section 407(d)(5)).

ERISA § 408(e), 29 U.S.C. § 1108(e) - Section 406 and 407 shall not apply to the acquisition or sale by a plan of qualifying employer securities (as defined in section 407(d)(5)) or acquisition, sale or lease by a plan of qualifying employer real property (as defined in section 407(d)(4)):

(1) if such acquisition, sale, or lease is for adequate consideration (or in the case of a marketable obligation, at a price not less favorable to the plan than the price determined under section 407(e)(1)),

(2) if no commission is charged with respect thereto, and

(3) if -

(A) the plan is an eligible individual account plan (as defined in section 407(d)(3)), or

(B) in the case of an acquisition or lease of qualifying employer real property by a plan which is not an eligible individual account plan, or of an acquisition of qualifying employer securities by such a plan, the lease or acquisition is not prohibited by section 407(a).

ERISA § 502(a), 29 U.S.C. § 1132(a) - A civil action may be brought:

(1) by a participant or beneficiary

(A) for the relief provided for in subsection (c) of this section, or

(B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan;

(2) by the Secretary, or by a participant, beneficiary or fiduciary for appropriate relief under section 409;

(3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this title or the terms of the plan, or (B) to obtain other appropriate equitable relief (1) to redress such violations or (ii) to enforce any provisions of this title or the terms of the plan;

(4) by the Secretary, or by a participant, or beneficiary for appropriate relief in the case of a violation of 105(c);

(5) except as otherwise provided in subsection (b), by the Secretary (A) to enjoin any act or practice which violates any provision of this title, or (B) to obtain

other appropriate equitable relief (i) to redress such violation or (ii) to enforce any provisions of this title;

(6) by the Secretary to collect any civil penalty under subsection (c)(2) or (i) or (1);

(7) by a State to enforce compliance with a qualified medical child support order (as defined in section 609(a)(2)(A));

(8) by the Secretary, or by an employer or other person referred to in section 101(f)(1), (A) to enjoin any act or practice which violates subsection (f) of section 101, or (B) to obtain appropriate equitable relief (i) to redress such violation or (ii) to enforce such subsection; or

(9) in the event that the purchase of an insurance contract or insurance annuity in connection with termination of an individual's status as a participant covered under a pension plan with respect to all or any portion of the participant's pension benefit under such plan constitutes a violation of part 4 of this title or the

terms of the plan, by the Secretary, by any individual who was a participant or beneficiary at the time of the alleged violation, or by a fiduciary, to obtain appropriate relief, including the posting of security if necessary, to assure receipt by the participant or beneficiary of the amounts provided or to be provided by such insurance contract or annuity, plus reasonable prejudgment interest on such amounts.

STATEMENT OF THE CASE

Arthur D. Little, Inc. ("ADL") is a Cambridge, Massachusetts based international consulting firm (A-26). The petitioner, Peter A. Crawford ("Crawford") began working at ADL as a Management Consultant on June 7, 1981 (A-26). In March 1988, ADL's Board of Directors voted to form an ESOP pursuant to 26 U.S.C. § 4975(e)(7) of the Internal Revenue Code and to propose a going-private transaction whereby ADL would (1) acquire for $60 per share all outstanding publicly held, minority shares of ADL stock then trading at $33 per share;[1] (2) cancel all existing shares of ADL stock; (3) reissue "New Shares" which were equivalent to .946288 Old Shares; and (4) sell a portion of the New Shares to the ESOP at $60 per share with financing from ADL (which in turn received bank financing) (A-26-27). Crawford objected to the transaction for a variety of reasons, and delivered to the Department of Labor a thirty-two page

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[1]Amended Complaint, ¶ 28, A-79.

memorandum detailing his belief that as part of the going-private transaction, the ESOP Trustees were intending to buy ADL common stock in "excess of adequate consideration" within the meaning of 29 U.S.C. § 1002(18) (A-27). Crawford urged the Department of Labor to seek an injunction enjoining ADL from consummating its plan (A-27). The Department of Labor declined Crawford's invitation, and on June 14, 1988, the ADL shareholders approved the proposed transaction (A-28). ADL loaned to the ESOP Trustees $32.8 million in order to purchase 546,520 New Shares of ADL common stock at $60 per share (A-28). The new ADL stock was deposited within the ESOP to be released over the next seven years on a pro rata basis to the individual accounts of qualified employee participants of the ESOP (A-28). ADL agreed to make tax deductible contributions to the ESOP sufficient to repay the principal and interest due ADL (and its banks) on the ESOP loan (A-28-29).

On November 30, 1988, Crawford was informed that due to budget cuts he was to be terminated (A-29). Crawford negotiated an extension of salary and benefits until March 24, 1989 with an unpaid 60 day leave thereafter (A-30). On May 12, 1989, Crawford filed his

initial complaint in this action *pro se* (A-30). Crawford then resigned from ADL effective May 18, 1989 (A-30). Plaintiff was cashed out from the ESOP pursuant to ESOP plan provisions on May 7, 1990 (A-30). On June 10, 1993, Crawford filed an amended complaint seeking recovery on behalf of the ESOP for breach of fiduciary duty by the Trustees who paid "excess" consideration for the new ADL shares (A-31). Plaintiff invoked jurisdiction in the District Court pursuant to 29 U.S.C. § 1132(e) [ERISA § 502(e)]. In his amended complaint, Crawford alleged that the ESOP Trustees (1) failed to negotiate with ADL concerning the diluted value of the New Shares purchased by the ESOP as a result of a 5.68% dividend granted to the Memorial Drive Trust "MDT" which controlled 70% of the ADL stock prior to the transaction (A-74), and (2) failed to consider the debt charges for financing the ADL stock purchase which would lower ADL's projected earnings, thus, prospectively reducing the value of the ADL common shares (A-74). Crawford also alleged in his amended complaint that the ESOP Trustees depended excessively upon the valuation conducted by Brian Freeman which (1) was based on overly optimistic financial projections, (2) failed to apply proper valuation principles in its

analysis, and (3) failed to consider the prices of similar transactions and values of publicly held companies (¶ 37, A-80-83). The District Court granted Crawford's Motion to Amend his Complaint on June 24, 1993 (A-32). The ESOP Trustees then renewed their motions for summary judgment. In opposition to the ESOP Trustees' motion for summary judgment, Crawford submitted expert reports of Robert Socol that demonstrated Mr. Freeman's analysis of the fair market value of the ADL stock was seriously flawed (A-89-110). The District Court granted defendants' motion for summary judgment by order dated October 12, 1993 (A-21). Crawford filed a timely notice of appeal to the First Circuit. On appeal, Crawford argued that he had standing because he was a current employee of ADL at the time he filed the lawsuit and alternatively as a former employee, he suffered a reduction in the amount of his vested benefits as a result of the purchase by the ESOP Trustees of overpriced stock. The First Circuit rejected Crawford's argument that he had standing as a current employee noting that he was not a current employee throughout the litigation. *Crawford v. LaMantia*, 34 F.3d 28, 32 (1st Cir. 1994) (citing *Sommers Drug Stores Co. Employee Profit Sharing Plan v.*

Corrigan, 883 F.2d 345, 348 (5th Cir. 1989)) (other citations omitted). The First Circuit also rejected Crawford's second argument that as a former employee he had suffered a reduction in benefits when the ESOP Trustees overpaid for the new ADL stock. In a statement that appears broadly applicable to all ESOP participants, the Court held:

> "Had defendants not overvalued the shares, they would not have borrowed as much money from ADL. Instead, a recalculation of the price of the stock would have resulted only in a smaller loan, lower principal and interest payments to be paid quarterly by ADL, and the same number of New Shares placed in the suspense account. It would *not* have resulted in a similar loan being made to the ESOP with any excess cash to be distributed to the accounts of the participants. The borrowed funds were not available for distribution; they were to be used *exclusively* to buy stock, or in the alternative, to pay back the loan."

Id. at 33. (Emphasis Supplied).

The First Circuit affirmed the lower Court by its decision dated September 14, 1994 (A-44). A request for rehearing and/or rehearing *en banc* was filed by Crawford on September 28, 1994. Accompanying Crawford's motion for rehearing, the Department of Labor moved for leave to enlarge the time for filing a Brief as Amicus

Curiae in Support of the Petitioner's Motion for Rehearing (A-58).[2] That leave was denied without reason on November 1, 1994 (A-47). The First Circuit also issued an errata sheet to its original decision of September 14, 1994 (A-59)[3] The Petitioner's request for a rehearing was denied November 29, 1994 (A-57).

ARGUMENT

A. CRAWFORD HAS STANDING TO BRING THIS ACTION BECAUSE HE HAS A COLORABLE CLAIM TO VESTED BENEFITS AND FALLS WITHIN THE ZONE OF INTERESTS ERISA WAS DESIGNED TO PROTECT.

Under section 502(a) of ERISA, 29 U.S.C. § 1132(a), participants have standing to bring suit to enforce ERISA's fiduciary

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[2] The Secretary of Labor in his motion at ¶ 3 stated that "this case raises an important issue relating to the proper construction of ERISA. Does an Employee Stock Ownership Plan ("ESOP") that pays more than adequate consideration for qualifying employer securities suffer a loss of plan assets within the meaning of ERISA § 409(a), 29 U.S.C. § 1109(a), where the ESOP purchases the securities with the proceeds of an exempt loan?"

[3] An additional sentence was added to FN6, p.11 of the original slip opinion distinguishing *Reich v. Valley Nat. Bank of Ariz.*, 837 F.Supp. 1259 (S.D.N.Y. 1993) from the case at bar (A-59 - A-60). But see ¶ 18, 19 of the Amended Complaint (A-75-76) where Crawford alleges that ADL lost $4.6 million the year in which the transaction occurred.

standards. "Participant" is defined under ERISA to include "any employee or former employee of an employer. . . who is or may become eligible to receive a benefit of any type from an employee benefit plan ERISA 3(7), 29 U.S.C. § 1002(7). The above statutory language was considered by the Supreme Court in *Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 117 (1989) when determining who was a participant under ERISA for the purpose of requiring disclosure of plan documents. The Supreme Court adopted a two-prong disjunctive test by holding that "participant" should be read to include employees in, or reasonably expected to be in, currently covered employment [the current employee test] or former employees who have. . . a reasonable expectation of returning to covered employment or who have a 'colorable claim' to vested benefits. Id.

Addressing first the second prong of the *Firestone* test, Crawford alleges that as a former employee he received reduced benefits as a result of the breach by the ESOP Trustees who paid too much for ADL stock to the detriment of each participant's account, including his own.[4] The ESOP's loss can be measured by the

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difference between the amount paid for the stock and its fair market value at the time of purchase. See *III Scott on Trusts* (4th ed. 1988) § 205 at 242 ("where the trustee is authorized to purchase property for the trust, and in breach of the trust he pays more than its fair value, he is chargeable with the amount that he paid in excess of the fair value"). As a participant whose account value was impaired by fiduciary misconduct, Crawford is entitled to a pro rata share of a recovery of that loss. Consequently, Crawford has a colorable claim to vested benefits within the meaning of *Firestone*.

In *Sommers Drug Stores Co. Employee Profit Sharing Trust v. Corrigan*, 883 F.2d 345, 347-50 (5th Cir. 1989), the Fifth Circuit held that the plaintiffs had standing to sue the trustees of a terminated profit sharing plan for violating their fiduciary obligations by selling the plan's stock to a party in interest for less than adequate consideration. The Court reasoned that the plaintiffs still had a colorable claim to benefits, even though they had already received lump sum

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[4] An ESOP is by definition under ERISA an individual account plan, ERISA § 3(34), 29 U.S.C. 1003 (34), where benefits are based solely upon the amount contributed to the participant's account and any income, expenses, gain and losses, and any forfeitures of accounts of other participants which may be allocated to such participant's account.

distributions, because the fiduciary breach had allegedly resulted in smaller distributions than they would otherwise have received. See *Kuper v. Quantum Chemical Corp.*, 829 F.Supp. 918 (S.D. Ohio 1993) (former participants in a terminated ESOP having standing to seek losses under ERISA based upon claims related to the diminution of the value of their stock). That finding is consistent with established trust law that if the "Trustee prior to the transfer of the trust property to the beneficiary incurred a liability for breach of trust, the transfer, although it terminates the trust of the property, does not discharge the trustee from his liability for the breach of trust." *Restatement (Second) of Trust § 342 (1959).* See also *Ruocco v. Bateman, Eichler, Hill, Richards, Inc.*, 903 F.2d 1232 (9th Cir.), *cert. denied*, 11 S.Ct. 254 (1990) (former participants had standing to compel payment of unallocated reserves); *Wright v. Bosch Trucking Co., Inc.*, 804 F.Supp. 1069 (C.D. Ill. 1992) (involuntarily terminated employee who accepted lump sum distributions deemed "participant" where portion of vested amount subject to possible divestment); *Amalgamated Clothing and Textile Workers' Union v. Murdock*, 861 F.2d 1406, 1417 (9th Cir. 1988) (claim for breach of fiduciary responsibility considered a 'benefit

of any type' justifying standing despite the distribution of vested benefits).

The First Circuit's decision on the facts of the present case is inconsistent not only with *Sommers* and *Kuper*, but also with its own decision in *Vartanian v. Monsanto*, 14 F.3d 697 (1st Cir. 1994). In *Vartanian*, the First Circuit adopted an expansive reading of ERISA's standing provisions which is wholly at odds with the Court's treatment of Crawford's claim in this case. In *Vartanian*, the Court held that the central inquiry in determining standing is whether the plaintiff falls within the "zone of interests" ERISA was designed to protect, rejecting a rigid application of the *Firestone* test, which had been developed outside the context of standing. Id. at 701-02.[5] The Court noted that "[i]n determining who is a 'participant' for purposes of standing, the definition found in 29 U.S.C. § 1002(7) must be read in the context of traditional concepts of standing, not in the context of adjudicating the ultimate issue of the merits of the plaintiffs' claim. . . ." Id. at 701

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[5] See also *Mullins v. Pfizer, Inc.*, 23 F.3d 663, 668 (2d Cir. 1994) where the Second Circuit expressly endorsed the *Vartanian* view as to standing.

(quoting *Astor v. International Business Machines Corp.* , 7 F.3d 533, 538-39 (6th Cir. 1993)). In adopting a broad reading of participant standing, the Court stressed ERISA's "intention to provide the full range of legal and equitable remedies available in both state and federal courts and to remove jurisdictional and procedural obstacles which in the past appear to have hampered effective enforcement of fiduciary responsibilities under state law for recovery of benefits due to participants."[6]

Accordingly, *Vartanian* held that a plaintiff had standing to sue his former employer for allegedly misleading him about the impending creation of a new plan which would have provided better benefits than the plan under which he ultimately retired. Although the plaintiff had retired and received a lump sum distribution of all his benefits under the old plan before he brought suit, he had been a participant in an employee benefit plan at the time of the alleged breach of ERISA's fiduciary obligations, and thus fell "squarely within the 'zone of interest' ERISA was designed to protect." Id.

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[6] Id. at 702 (quoting S. Rep. No. 127, 93d Cong., 2d Sess., 3 (1974) reprinted in 1974 U.S.C.C.A.N. 4639, 4871).

In the present case, Crawford alleges that the ESOP trustees purchased employer stock at an inflated price in violation of ERISA's prohibited transaction provisions (ERISA § 406(a), 29 U.S.C. § 1106(a)) (A-80) and in breach of the fiduciaries duties of prudence and loyalty (ERISA § 404(a)1), 29 U.S.C. § 1104(a)(1)), at a time (June, 1988) when Crawford was unquestionably a participant in the ESOP. As a result Crawford and the other ESOP participants suffered a reduced level of benefits.[7] Under *Vartanian*'s reasoning, Crawford falls within ERISA's zone of interests and has standing to bring this suit.

B. THE ESOP AND ITS PARTICIPANTS, INCLUDING THE PLAINTIFF, SUFFERED A LOSS IF THE ADL STOCK WAS OVERPRICED.

The First Circuit, when presented with the issue of whether ESOP trustees that borrow funds from the employer to purchase stock of the employer at a price higher than the fair market value have

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[7] The First Circuit erred in its attempt to distinguish its holding in *Vartanian* from its holding in the case at bar *Crawford v. LaMantia*, 34 F.3d 28, 33 n.7 (1st Cir. 1994). Crawford's share of the recovery to the ESOP constitutes a claim for vested benefits.

breached their fiduciary duties to the plan participants, adopted a discredited legal theory; the "no loss" theory.[8]

According to the Court, "Had the trustees not overvalued the ADL shares, the trustees would have borrowed less from ADL. A downward recalculation of the price of stock [to reflect fair market value] would have resulted in a smaller loan, lower principal and interest payments. . .and the same number of New Shares placed in the suspense account." As there was no obligation to distribute any excess cash [from the overvaluation] to the accounts of the participants, the plaintiff [and other participants] suffered no loss. *Crawford v. LaMantia*, 34 F.3d 28, 33 (1st Cir. 1994). Stated otherwise, such trustees can pay whatever price they want for the employer stock regardless of specific ERISA requirements such as (1) investing the assets for the exclusive benefit of participants and beneficiaries, ERISA § 404(a)(1)(A) and (B), 29 U.S.C. § 1104(a)(1)(A) and (B); (2) permitting a sale or exchange between the ESOP and "party in interest," ERISA § 406(a)(1)(A), 29 U.S.C. § 1106 (a)(1)(A); [only if]

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[8] See *Reich v. Valley Nat. Bank of Ariz.*, 837 F. Sup 1259, 1284 (S.D. N.Y., 1993).

the securities are qualified employer securities acquired for "adequate consideration", ERISA § 408(e), 29 U.S.C. § 1108(e), and (3) providing for any agreement that relieves a fiduciary from any responsibility, ERISA § 410(a), 29 U.S.C. § 1110(a).

To date, no other circuit has adopted such a theory. In fact, in all circuits that have ruled on the issue, each has adopted legal reasoning that lies in direct conflict with the First Circuit's "no loss" theory. In *Donovan v. Cunningham*, 716 F.2d 1455 (5th Cir. 1983), *cert. denied*, 467 U.S. 1251 (1984), the Fifth Circuit ruled that fiduciaries of an ESOP, which was part of an LBO transaction, breached their fiduciary duties under ERISA by purchasing certain stock on behalf of the ESOP for more than adequate consideration as defined by ERISA § 3(18). Id. at 1473-74. In so holding, the Fifth Circuit stressed that "ESOP fiduciaries will carry their burden to prove that adequate consideration was paid by showing that they arrived at their determination of fair market value by way of a prudent investigation in the circumstances then prevailing." Id. at 1467-68.

In *Reich v. Valley Nat. Bank of Ariz.* , the Southern District Court of New York, faced with overvaluation of stock in a leveraged buyout transaction, soundly rejected the "no loss" theory by holding:

> "Valley's argument that no loss could have been occasioned by the LBO transaction goes counter to ERISA's fiduciary standards and raises the dangers warned of by Congress. Congress clearly believed that a leveraged ESOP investing in employer securities was investing plan assets that were subject to possible loss. Valley's position would lead, logically, to a conclusion that would eviscerate the congressional intent behind the protections enacted for the benefit of plan participants; the conclusion that an ESOP could participate in the leveraged buyout of the sponsoring entity and pay any price per share possible, without suffering any loss no matter how dear the price. This argument renders the 'adequate consideration' protection of 29 U.S.C. § 1108(e) a nullity. Congress clearly felt otherwise.

Reich v. Valley Nat. Bank of Ariz., 837 F.Supp. 1259, 1287 (S.D.N.Y. 1993) (emphasis added).

Like *Reich*, all district courts to rule on the issue have held that an ESOP fiduciary's purchase of stock for more than "adequate consideration" gives rise to a valid ERISA claim under its fiduciary duty sections. See *Hood v. Smith's Transfer Corp.*, 762 F.Supp. 1274 (W.D. Kentucky 1991); *Brumfield v. Shelton*, 727 F.Supp. 282 (E.D.

La. 1989); *Ershick v. United Missouri Bank of* Kansas City, 1990 WL 126929 (D. Kan. 1990).

The Court's holding that the plaintiff is unharmed even if the ADL stock was overpriced is fundamentally at odds with ERISA's text. ERISA *prohibits* fiduciaries from causing ESOPs to purchase stock sold by a party in interest (including a sponsoring employer such as ADL)[9] unless the transaction is for "adequate consideration" within the meaning of a statutory exemption set forth in Section 408(e) of the statute, 29 U.S.C. § 1108(e).[10] "Adequate consideration" is defined as "the fair market value of the asset as determined in good faith by the trustee or named fiduciary. . . ." ERISA § 3(18), 29 U.S.C. § 1002(18). Thus, ERISA permits ESOP fiduciaries to purchase employer stock only if they can demonstrate that the stock was purchased for fair market value as determined "by way of a prudent investigation in the

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[9]*See* ERISA § 3(14)(C), 29 U.S.C. § 1002(14)(C).

[10] ERISA § 406(a)(1)(A), 29 U.S.C. § 1106(a)(1)(A), prohibits fiduciaries from causing any "sale or exchange" of property between a plan and a "party in interest", and ERISA § 406(a)(1)(D), 29 U.S.C. § 1106(a)(1)(D) prohibits fiduciaries from causing the assets of a plan to be transferred to, or used by or for the benefit of, any "party in interest." Under these provisions, the stock purchase was prohibited unless exempt under Section 408(e), 29 U.S.C. § 1108(e).

circumstances then prevailing." *Donovan v. Cunningham*, 716 F.2d 1455, 1467-68 (5th Cir. 1983), *cert. denied*, 467 U.S. 1251 (1984).

Congress also emphasized the importance of paying the appropriate price for employer securities in the legislative history of Section 408(b)(3), 29 U.S.C. § 1108(b)(3), which provides an exemption from ERISA's prohibited transaction provisions for loans made to ESOPs primarily for the benefit of the plans' participants and beneficiaries at reasonable interest rates. In the legislative history of the exemption, Congress expressed its concern that in leveraged ESOP transactions "the purchase price of the stock from the party-in-interest should not be too high, so that plan assets might be drained off" and, accordingly, directed the Secretary of Labor[11] to give "special scrutiny to such transactions". H.R. Rep. No. 1280, 93d Cong., 2d Sess. (1974) at 313, reprinted in 1974 U.S. Code Cong. & Admin. News 5038, 5093.

The Act and its legislative history make clear that the fiduciaries of the ESOP have the obligation to ensure that the ESOP

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[11] See also ¶ 3 of Motion of the Secretary of Labor for Enlargement of Time in which to File a Brief Amicus Curiae In Support of Petition for Rehearing (A-49).

did not spend more on ADL's stock than the stock was worth. It makes little sense to require plan fiduciaries to prudently investigate the stock's value and pay no more than fair market value, if participants are unharmed regardless of the price paid. The text of ERISA cannot be squared with a holding that would permit fiduciaries to purchase employer stock at any price, no matter how high, and immunize trustees from participant lawsuits seeking recovery of the loss resulting from excessive payments.

Under a plain reading of the statute, the participants of the ESOP suffered a loss if the stock was overvalued. In this case the defendants committed the ESOP to purchase 546,520 shares of ADL stock for $60 a share (A-28). The stock was deposited in the ESOP's suspense account to be released to individual participants' accounts over a seven year period as the ESOP paid back the loan (A-28). If the stock was not worth the $60 per share paid for it, the participants, including the plaintiff, ultimately received fewer shares or less valuable stock than they should have received, and the ESOP suffered a loss.

Nevertheless, the Court held that the plaintiff failed to show any injury even if the stock were overpriced, reasoning that if the parties had properly valued the stock, they would simply have entered into a different transaction involving a smaller loan, lower employer contributions, and the same number of shares being held by the ESOP.[12]

The Court's analysis is in error because it fails to give effect to ERISA's adequate consideration requirement. When the defendants committed the ESOP to purchase ADL's stock, they had an obligation to observe ERISA's commands. See *Reich v. Valley Nat. Bank of Ariz.*, 837 F.Supp. 1259, 1287-88 (S.D.N.Y. 1993) (". . . "while an employer is under no obligation to establish an ESOP, once it does so ERISA's standards apply. An employer cannot condition Plan contributions on a violation of ERISA. . . ."). ERISA compelled the fiduciaries to buy

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[12] The petitioner does not know the basis of the Court's supposition that the parties would have simply entered into a different transaction with a smaller loan, lower contributions and the same number of shares. There is no evidence in the record to support this conclusion and the District Court made no such finding. The issue was not even discussed during oral argument. Furthermore, nothing in ERISA would have prohibited the ESOP trustees from receiving more stock or other considerations if the stock alone were overpriced.

the stock for its fair market value. The defendants were not free to disregard ERISA's requirements on the theory that the parties would never have agreed to the transaction on the same terms if they had been compelled to give the participants stock worth the amount paid, as required by ERISA. The plan's participants were entitled to the benefit of the bargain. If the plan's assets were expended (or "drained off") for overpriced stock, they suffered a loss. In this case, Crawford, a vested participant, received a diminished distribution of plan benefits for just this reason. As a result, he has a claim under ERISA and standing to bring that claim.

C. AN EMPLOYEE WHO WAS A PARTICIPANT IN THE PLAN AT THE TIME OF THE BREACH BY THE ESOP TRUSTEES AND A CURRENT EMPLOYEE AT THE TIME THE LAWSUIT WAS INSTITUTED BUT HAS SINCE TERMINATED EMPLOYMENT HAS STANDING TO SUE THE ESOP'S TRUSTEES FOR PAYING MORE THAN ADEQUATE CONSIDERATION.

In dismissing Crawford's argument that he had standing as a current employee, the First Circuit, citing *Sommers Drug Stores Co.*

Employee Profit Sharing Plan v. Corrigan, 883 F.2d 345, 348 (5th Cir 1989), stated:

> . . . "although plaintiff may have had standing as a current employee when he brought this action, by the time he filed his amended complaint, he lost his standing on account of having terminated his employment with ADL and having collected all vested benefits then due him [without regard to the alleged overpayment by the ESOP trustees] from the ESOP."

Crawford v. LaMantia, 34 F.3d 28, 32 (1st Cir. 1994).

In determining whether for purposes of standing a current employee must maintain that status throughout the litigation, petitioner urges the Supreme Court to consider its own decision with respect to an analogous issue in *Gollust v. Mendell*, 111 S.Ct. 2173 (1991).

In *Gollust*, the plaintiff/shareholder instituted a § 16(b) insider trading action on behalf of the corporation alleging that the defendants were liable to the corporation for $11 million in profits earned by the defendants from trading stock in the corporation. Id. at 2176. After the commencement of the action, the corporation was acquired by another corporation and the shareholders, including the plaintiff, exchanged their shares in the original corporation for shares in the new

corporation. Id. The United States District Court for the Southern District of New York granted the defendants' motion for summary judgment on the basis that plaintiff no longer had standing because after the take over, the plaintiff no longer held stock in the corporation. Id. at 2177. The United States Court of Appeals for the Second Circuit reversed. *Mendell v. Gollust*, 909 F.2d 724, 731 (2d Cir. 1990). The United States Supreme Court affirmed the reversal holding that it was not necessary for the plaintiff to continue to hold stock of the issuer in order to maintain his insider trading action where he had a financial stake in the parent corporation. Id.

As in the present situation, the plaintiff in *Gollust* had standing at the initiation of the action. As in the present situation, the status of the plaintiff in *Gollust* was altered after the commencement of the litigation. As in the present situation, the change in status of the plaintiff was involuntary. The Supreme Court emphasized this fact. It noted that the "danger of such intentional restructuring to defeat the enforcement mechanism incorporated in the statute is clearly present." Id. at 2177 n. 5 (quoting *Mendell v. Gollust*, 909 F.2d 724, 731 (2d Cir. 1990)). Finally, in each case, the plaintiff had an economic interest in

the outcome. In *Gollust,* that interest was in the recovery of insider profits, and in the case at bar, that interest was in the recovery of the pro rata share of the overpayment.

Crawford's maintenance of this action is "not barred by the language of the statute or by existing case law, and it is fully consistent with the statutory objectives" and therefore the lower court erred in granting summary judgment in favor of the Respondents. *Gollust v. Mendell,* 111 S.Ct. 2173, 2177 (1991).

CONCLUSION

For all reasons set forth above, the petitioner requests that this Court grant this Petition for Writ of Certiorari.

Respectfully submitted,

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